

for refusing to treat CAP charges exogenously is no longer valid.<sup>637</sup>

339. MCI advocates permitting AT&T to treat endogenously the reduction in its access costs resulting from changing access providers, but requiring AT&T to treat as exogenous any changes in the rates that a current access provider charges, regardless of whether the current provider is a LEC or a CAP. MCI argues that this would encourage AT&T to be efficient in its selection of access providers, but not penalize AT&T for access cost changes outside its control after it has selected its provider.<sup>638</sup> MCI also contends that requiring AT&T to pass through the savings resulting from changing access providers would lessen AT&T's incentive to switch access providers, thereby strengthening the LECs' current monopoly of the transport market.<sup>639</sup>

340. As for other issues, some of the LECs argue that the Commission should permit the LECs the same pricing flexibility that it allows their competitors, i.e., to offer bundled services and equipment, volume and term discount plans, and a range of rates in their tariff filings.<sup>640</sup> SWB asserts that the current asymmetrical treatment regarding pricing flexibility denies price cap LECs equal protection under the law.<sup>641</sup> A number of carriers assert that they are placed at a competitive disadvantage because their rate structures are dictated by the Part 69 access charge rules, and their competitors are free to adopt any rate structure they choose.<sup>642</sup> Many carriers also request reduced notice periods for LEC price cap tariff filings.<sup>643</sup> Many LECs also contend that the cost support, demand information, service quality reports, and other similar reporting requirements

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<sup>637</sup> US West Comments at 60-61, citing AT&T Price Cap Order, 4 FCC Rcd at 3029; Ameritech Comments at 28; Pac Bell Comments at 66.

<sup>638</sup> MCI Comments at 57-58.

<sup>639</sup> MCI Reply at 68-69.

<sup>640</sup> Bell Atlantic Reply at 27; USTA Comments at 90; SNET Comments at 11; Pac Bell Comments at 66; Lincoln Comments at 5; NYNEX Comments at 52; Bell Atlantic Comments at 23; SWB Comments at 56; Ameritech Comments at 28; RTC Comments at 16.

<sup>641</sup> SWB Comments at 56.

<sup>642</sup> USTA Comments at 90; Lincoln Comments at 5; SWB Comments at 56; BellSouth Comments at 67.

<sup>643</sup> USTA Comments at 90; Lincoln Comments at 5; NYNEX Comments at 52; Bell Atlantic Comments at 23; SWB Comments at 57.

unfairly provide their competitors with market intelligence about networks, costs, and customers.<sup>644</sup> USTA, SWB, and CSE contend that, while LEC depreciation rates are established by Commission proceeding, LEC competitors are permitted to set their own depreciation rates.<sup>645</sup>

341. Some commenters suggest that all interstate access providers (and not just the LECs) should be required to provide the Commission with a description of their geographic service areas and a list of their services, to enable the Commission to assess the level of competition in local exchange markets.<sup>646</sup> Similarly, Pac Bell claims that the distinction the Commission made between nondominant and dominant carriers in CC Docket No. 93-36 is not based on evidence from actual markets. Pac Bell avers that an examination of markets by service and geography would have shown that in some metropolitan markets the LECs are not dominant.<sup>647</sup>

342. Ad Hoc, TCG, MCI, Sprint, and MFS assert that the Commission should not equalize LEC and CAP treatment as long as the LECs still retain market dominance and control over essential facilities and resources.<sup>648</sup> MCI argues that, if regulation is eased before local service and access providers can establish themselves within the market, the LECs will be able to thwart emerging competition.<sup>649</sup> MCI also recommends that, if the Commission requires the CAPs to file reports disclosing customer-specific marketing plans, such reports should be given

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<sup>644</sup> GTE Reply at 74; USTA Comments at 91; Pac Bell Comments at 56-58; SWB Comments at 63; US West Comments at 50.

<sup>645</sup> USTA Comments at 91; SWB Comments at 57; CSE Reply at 4.

<sup>646</sup> USTA Comments at 91; Pac Bell Comments at 69; SWB Comments at 59; US West Comments at 64.

<sup>647</sup> Pac Bell Comments at 66-67, citing Tariff Filing Requirements of Nondominant Common Carriers, CC Docket No. 93-36, 8 FCC Rcd 6752 (1993) (Nondominant Tariff Requirements Order). In that Order, the Commission amended its rules to allow domestic nondominant carriers to state in their tariffs a reasonable range of rates. Those rules were later struck down by the Court of Appeals for the District of Columbia Circuit. *Southwestern Bell Corp. v. FCC*, 1995 WL 19336 (D.C. Cir., decided Jan. 20, 1995).

<sup>648</sup> Ad Hoc Comments at 31; MFS Comments at 33; MCI Comments at 59; Sprint Comments at 22; TCG Comments at 14.

<sup>649</sup> MCI Reply at 71.

proprietary treatment.<sup>650</sup>

### 3. Analysis

343. When we last reviewed the exogenous treatment of AT&T access costs in the AT&T Performance Review, we recognized that this difference in treatment of LEC and CAP access charges could have the effect of biasing competition among access providers. We declined to revise the rule, nonetheless, as several LECs recommended. We noted that almost all of AT&T's Basket 2 and Basket 3 services have been removed from price cap regulation.<sup>651</sup> This reduces the likelihood that any actual bias exists, because the services remaining under price cap regulation are in Basket 1, and those services use LEC switched access services almost exclusively.<sup>652</sup> Finally, we concluded that there was no evidence to indicate that making exogenous cost changes to reflect changes in CAP access rates would have any effect on AT&T's Basket 1 PCI, and thus have no effect on AT&T's incentives.<sup>653</sup>

344. Similarly, no evidence has been submitted in the record of this proceeding that demonstrates that AT&T's use of CAP access to provide Basket 1 services is more than de minimis. Consequently, we cannot conclude at this time that reflecting changes in CAP access rates as exogenous cost adjustments to AT&T's Basket 1 PCI would have any measurable effect on that index or affect AT&T's incentives to choose either a LEC or a CAP for its access provider. We also cannot conclude that exogenous treatment of LEC access rates creates any actual bias in the development of switched transport competition. Accordingly, we continue to find no basis for concluding that the current rule should be modified. We may revisit this issue in the future, however, as competition in the provision of switched transport service develops.

345. In the Notice, in addition to the baseline issues we discuss here, we solicited comment on six "transition issues," to develop data and information relevant to fashioning a workable plan for revising LEC price cap regulation as competition in the market for access services develops.<sup>654</sup> As we discuss above, we also intend to issue a further notice of proposed rulemaking to solicit further comment on a number of transition issues,

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<sup>650</sup> Id.

<sup>651</sup> AT&T Performance Review, 8 FCC Rcd at 5169.

<sup>652</sup> Id.

<sup>653</sup> Id.

<sup>654</sup> Notice, 9 FCC Rcd at 1705-06.

including whether any particular price cap rules or policies should be revised as competition develops in local exchange markets. Because the upcoming further notice proceeding can examine more thoroughly the proposals for equalizing LEC and CAP regulation, we will not address the merits of these proposals here.

346. Finally, we note that, since this proceeding was initiated, the Commission has addressed the concern expressed here by several commenters that all interstate access providers should provide information to the Commission that would enable us to assess the level of competition in the local exchange markets. In the Virtual Collocation Order, we delegated authority to the Common Carrier Bureau to initiate a monitoring program to enable us to monitor the development of competition in interstate access markets.<sup>655</sup> As for Pac Bell's assertion that we did not distinguish between "dominant carrier" and "nondominant carrier" correctly in the Nondominant Tariff Requirements Order, we specifically declined in that Order to revise the definition of dominance developed in the Competitive Carrier proceeding.<sup>656</sup> The Commission in the Nondominant Tariff Requirements Order intended only to revise the tariff filing requirements in light of the Court decision invalidating our "forbearance" rules,<sup>657</sup> not to revisit the definition of "nondominant carrier" itself.<sup>658</sup> To the extent that Pac Bell requests us to reconsider any conclusion we reached in the Nondominant Tariff Requirements

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<sup>655</sup> Expanded Interconnection with Local Telephone Company Facilities, CC Docket No. 91-141, 9 FCC Rcd 5154, 5177 (1994) (Virtual Collocation Order).

<sup>656</sup> Nondominant Tariff Requirements Order, 8 FCC Rcd at 6754. See Policy and Rules Concerning Rates for Competitive Common Carrier Services and Facilities Authorizations Therefor, CC Docket No. 79-252, First Report and Order, 85 FCC 2d 1 (1980) (First Report); Second Report and Order, 91 FCC 2d 59 (1982) (Second Report); Third Report and Order, 48 Fed. Reg. 46,791 (1983) (Third Report); Fourth Report and Order, 95 FCC 2d 554 (1983) (Fourth Report), vacated sub nom. AT&T v. FCC, 978 F.2d 727 (D.C. Cir. 1992), reh. en banc denied, January 21, 1993; Fifth Report and Order, 98 FCC 2d 1191 (1984), recon. 59 Rad. Reg. 2d 543 (1985); Sixth Report and Order, 99 FCC 2d 1020 (1983) (Sixth Order), reversed sub nom. MCI v. FCC, 765 F.2d 1186 (D.C. Cir. 1985) (Competitive Carrier).

<sup>657</sup> Id., citing AT&T v. FCC, 978 F.2d 727 (D.C. Cir. 1992) (Forbearance Decision), cert. denied, 113 S.Ct. 3020 (1993). Under the forbearance rules, the Commission permitted nondominant carriers to provide service without filing tariffs.

<sup>658</sup> Nondominant Tariff Requirements Order, 8 FCC Rcd at 6754.

Order, this is not the appropriate proceeding to do so.

**E. The Inflation Measure: GNP-PI or GDP-PI**

347. The Commission's price cap formula for LECs uses the U.S. Department of Commerce, Bureau of Economic Analysis' 45-day estimate of the Gross National Product Price Index (GNP-PI) as its inflation measure.<sup>659</sup>

348. USTA and several LECs recommended that the Commission replace the GNP-PI with the Gross Domestic Product Price Index (GDP-PI).<sup>660</sup> As explained by SWB, the GNP-PI is based upon production by U.S. firms, including overseas production, while the GDP-PI excludes overseas production by U.S. firms and includes domestic production by foreign-owned firms.<sup>661</sup> Data provided by SWB and USTA demonstrate that, from 1982 to 1993, there has been only a slight difference between the GNP-PI and the GDP-PI.<sup>662</sup>

349. The commenters state that, beginning in 1991, the U.S. Department of Commerce discontinued publication of the 45-day estimate of the GNP-PI, substituting for it a 45-day estimate of the GDP-PI.<sup>663</sup> They further state that estimates of the GNP-PI are not released timely enough for the LECs to incorporate them in their annual access tariff filings.<sup>664</sup> As a result, the commenters assert that most LECs now use the 45-day GDP-PI estimate in their annual access tariff filings and then adjust it when the GNP-PI figures become available.<sup>665</sup>

350. The commenters argue that replacing the GNP-PI with the GDP-PI would eliminate an unnecessary administrative burden

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<sup>659</sup> Sections 61.3(p) and 61.45(c) of the Commission's Rules, 47 C.F.R. §§ 61.3(p), 61.45(c); 5 FCC Rcd at 6793.

<sup>660</sup> USTA Comments at 95-96; NYNEX Comments at 66-67; Pac Bell Comments at 34-35; BellSouth Comments at 71; SWB Comments at 65-67.

<sup>661</sup> SWB Comments at 65; USTA Comments at 96.

<sup>662</sup> Pac Bell Comments at 35; NYNEX Comments at 66; SWB Comments at 66; USTA Comments at 96.

<sup>663</sup> NYNEX Comments at 66; USTA Comments at 95; SWB Comments at 65; BellSouth Comments at 71.

<sup>664</sup> NYNEX Comments at 66-67; USTA Comments at 95; SWB Comments at 65; BellSouth Comments at 71.

<sup>665</sup> NYNEX Comments at 67; USTA Comments at 95; SWB Comments at 66; BellSouth Comments at 71.

and have no material effect on the price cap indexes.<sup>666</sup> No commenting parties opposed this change.

351. We find that the substitution of GDP-PI for GNP-PI in the price cap formula will eliminate a needless administrative burden without causing any harm to the public. We, therefore, adopt this revision to the LEC price cap plan.

#### **F. Service Quality, Infrastructure Monitoring and Network Reliability**

##### **1. Background**

352. The Commission concluded in adopting price cap regulation for LECs that the increased profits available under this form of regulation would create investment incentives that would promote the development of high quality, innovative services and an advanced telecommunications infrastructure.<sup>667</sup> At the same time, we recognized our responsibility to ensure that cost-cutting by price cap carriers did not instead lead to degraded service and diminished investment in network modernization. We therefore expanded our monitoring of service quality and infrastructure development in order to ensure continued high quality service to ratepayers.<sup>668</sup>

353. The Commission requires all price cap LECs to file quarterly service quality reports and all mandatory price caps LECs to file semi-annual service quality reports and annual infrastructure reports.<sup>669</sup> In addition, the Commission has adopted network reliability reporting requirements that apply to all carriers. These rules require, inter alia, local exchange or interexchange common carriers or competitive access providers operating either transmission or switching facilities to notify the Commission within 120 minutes if they experience service outages potentially effecting 50,000 or more customers and lasting 30 or more minutes and within three days if they experience service outages potentially effecting 30,000 to 50,000

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<sup>666</sup> NYNEX Comments at 67; USTA Comments at 95-96; SWB Comments at 66-67; BellSouth Comments at 71; Pac Bell Comments at 35.

<sup>667</sup> LEC Price Cap Order, 5 FCC Rcd at 6827.

<sup>668</sup> LEC Price Cap Order, 5 FCC Rcd at 6827, 6829-30, Order on Reconsideration, 6 FCC Rcd at 2717-19.

<sup>669</sup> LEC Price Cap Order, 5 FCC Rcd at 6827-39.

customers.<sup>670</sup> The Commission investigates all such reported outages.

354. The quarterly service quality report includes information regarding installation and repair intervals for interexchange access and local service, trunk, blockage, switch downtime, and service quality complaints filed with state or federal regulatory authorities.<sup>671</sup> We require price cap LECs to file their quarterly service quality reports by study area,<sup>672</sup> and to disaggregate data within the report by MSA and non-MSA for purposes of (1) local service installation and repair intervals, (2) switch downtime, and (3) service quality complaints.<sup>673</sup> We also require price cap LECs to disaggregate switch downtime data by switch size (number of lines served), and to report fully switch downtimes of two minutes or more and to identify the individual switch involved in the incident. In addition, we require price cap LECs to disaggregate interexchange access installation and repair intervals data by special access and switched access.<sup>674</sup> The semi-annual service quality report is filed by study area, and contains information concerning customer satisfaction, dial tone response and transmission quality.<sup>675</sup>

355. The annual infrastructure report<sup>676</sup> provides

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<sup>670</sup> Section 63.100 of the Commission's Rules, 47 C.F.R. § 63.100; Amendment of Part 63 of the Commission's Rules to Provide for Notification by Common Carriers of Service Disruptions, 7 FCC Rcd 2010, 2010 (1992) (Service Outage Order), recon. denied and granted, Memorandum Opinion and Order and Further Notice of Proposed Rulemaking, 8 FCC Rcd 8517 (Service Outage FNPRM) (1993); Second Report and Order, 9 FCC Rcd 3911 (1994).

<sup>671</sup> Modified Service Quality Order, 8 FCC Rcd 7259, Attachment, FCC Report 43-05.

<sup>672</sup> A study area usually consists of a telephone company's service territory in a given state, although telephone companies occasionally have more than one study area in a particular state.

<sup>673</sup> Modified Service Quality Order, 8 FCC Rcd 7259, Attachment, FCC Report 43-05.

<sup>674</sup> Id.

<sup>675</sup> Modified Service Quality Order, 8 FCC Rcd 7259, Attachment, FCC Report 43-06.

<sup>676</sup> The LECS are required to file their service quality and infrastructure reports in the Automated Reporting Management Information System (ARMIS) format. See Automated Reporting Requirements for Certain Class A and Tier 1 Telephone Companies

information relating to switching equipment, transmission facilities, LEC call set-up time, access lines in service, access line gain, and total gross capital expenditures.<sup>677</sup> We require the mandatory price cap LECs to file infrastructure reports by study area and to disaggregate switching equipment data by MSA and non-MSA.<sup>678</sup>

356. In the Notice, we observed that the monitoring data indicated that service quality under price caps was largely comparable to the levels achieved under rate-of-return regulation, although there were some possible problems.<sup>679</sup> We requested comment on whether the Commission should increase or revise the monitoring of the LECs' network reliability, service quality and infrastructure development. We also solicited comment on whether, and if so how, the Commission should expand its service quality monitoring to include price cap LEC facilities and services that may be interconnected with the local exchange network or used to provide similar capabilities, including wireless services and coaxial cable.<sup>680</sup>

## 2. Comments

357. MCI and Ad Hoc state that continued service quality monitoring is important, but recommend no changes to the current procedure.<sup>681</sup> Sprint, NYNEX and RTC state that the Commission's current monitoring system is adequate and that no additional reporting requirements are warranted.<sup>682</sup>

358. USTA and several of the LECs assert that, as markets become more competitive, competitive pressures will force the LECs to maintain high service quality and the need for service quality monitoring will diminish. They suggest that reporting requirements should be relaxed after markets have become more

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(Parts 31, 43, 67 and 69 of the FCC's Rules), CC Docket No. 86-182, Report and Order, 2 FCC Rcd 5770 (1987), modified on recon., 3 FCC Rcd 6375 (1988).

<sup>677</sup> Modified Service Quality Order, 8 FCC Rcd 7259, Attachment, FCC Report 43-07.

<sup>678</sup> Id.

<sup>679</sup> Notice, 9 FCC Rcd at 1691.

<sup>680</sup> Notice, 9 FCC Rcd at 1700-01.

<sup>681</sup> MCI Comments at 50-51; Ad Hoc Comments at 27-28.

<sup>682</sup> Sprint Comments at 20; NYNEX Comments at 56; RTC Comments at 22-23.



competitive.<sup>683</sup> A number of LECs express the concern that they would be disadvantaged by unequal reporting requirements in a competitive environment and argue that reporting requirements should be the same for all competitors.<sup>684</sup>

359. TCA notes that, although a survey of its members suggests that overall levels of service quality have not suffered under price cap regulation, many of its members reported disparities in service quality and availability among geographic locations. It suggests that the Commission should enhance its service quality monitoring program by requiring identification of poorly performing wire centers and underserved areas, and by collecting information on data transmission quality.<sup>685</sup>

360. USTA and several LECs argue that any benefits associated with TCA's recommendation would be outweighed by the additional costs and burdens that would result from increased reporting requirements.<sup>686</sup> USTA argues that the facts do not support TCA's claim that rural areas are falling behind urban areas in service quality. For example, USTA notes that, on an overall basis, non-MSA areas have a higher percentage of lines served by digital switches than MSA areas.<sup>687</sup> The parties opposing TCA's suggestion note that the Commission has previously rejected similar proposals by TCA,<sup>688</sup> and that it would impose significant burdens on both price cap LECs and the Commission.<sup>689</sup>

361. Pac Bell states that infrastructure monitoring of

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<sup>683</sup> USTA Comments at 92-93; BellSouth Comments at 59; US West Comments at 50; SWB Comments at 63; Ameritech Comments at 20. See also SNET Comments at 4-5 (reporting requirements should be eliminated after a specified period of time); Lincoln Comments at 14 (service quality reporting requirements should be eliminated).

<sup>684</sup> Ameritech Comments at 20; BellSouth Comments at 59; US West Comments at 50; Pac Bell Comments at 57; GTE Comments at 79.

<sup>685</sup> TCA Comments at i-iii, 1-11.

<sup>686</sup> USTA Reply at 68-71; NYNEX Reply at 62-65; Pac Bell Reply at 55-59; US West Reply at 37-41; SWB Reply at 75-79.

<sup>687</sup> USTA Reply at 70-71.

<sup>688</sup> USTA Reply at 68-69, citing Policy and Rules Concerning Rates for Dominant Carriers, Memorandum Opinion and Order, 8 FCC Rcd 7474, 7476 (Service Quality Modifications Order) (1993); NYNEX Reply at 62-63; Pac Bell Reply at 55-56; US West Reply at 40; SWB Reply at 76.

<sup>689</sup> USTA Reply at 69-70.

carrier networks could be expanded to include additional items as new technologies are deployed. For example, Pac Bell suggests that Table I of the Infrastructure Report for Switching Equipment could be expanded to include the number of local switches equipped with Advanced Intelligent Network capabilities, Synchronous Optical Network interfaces and the number of lines served by those switches.<sup>690</sup> US West asserts that Pac Bell's proposed modifications are burdensome and redundant. As an example, it states that Pac Bell's proposed expansion of Table II, ARMIS 43-07, appears to duplicate data contained in the Commission's comprehensive report on fiber deployment.<sup>691</sup>

362. ICA supports proposals to improve the reporting procedures for service outages.<sup>692</sup> It recommends that, in order to make most efficient use of the Commission's resources, service quality, network reliability and associated reporting requirements should be addressed outside of price caps and should be dealt with in the proceedings specially focused on those issues.<sup>693</sup>

363. None of the commenting parties recommends that the Commission should expand its service quality monitoring to include new facilities and services, such as wireless and coaxial cable, that a price cap LEC may interconnect with its local interexchange network or introduce as a separate, new service.<sup>694</sup>

364. Pac Bell recommends that service quality reporting of telephone service be kept separate from other services, such as broadband. It notes that video services are not as critical to the customer as basic telephone service and that a LEC would not control all of the elements of a video product offering.<sup>695</sup>

### 3. Analysis

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<sup>690</sup> Pac Bell Comments at 56-57.

<sup>691</sup> US West Reply at 37-38.

<sup>692</sup> ICA Comments at 18, citing Amendment of Part 63 of the Commission's Rules to Provide for Notification by Common Carriers of Service Disruptions, Notice of Proposed Rulemaking, 8 FCC Rcd 8517.

<sup>693</sup> ICA Comments at 18-19.

<sup>694</sup> See NYNEX Comments at 59; Ameritech Comments at 21; MCI Comments at 52.

<sup>695</sup> See Pac Bell Comments at 58-59 (specifying differences in service quality parameters as between broadband service and basic telephony).

365. There is nothing in the record to indicate that there has been any significant degradation of service quality since the institution of price cap regulation for LECs. Likewise, the record does not demonstrate that price cap regulation has created a disincentive for investment in the nation's telecommunications network. The service quality and infrastructure monitoring systems may nonetheless need updating and improving to keep pace with the introduction of new technologies and services and the development of competition. We recognize that, when the Bureau declined to adopt TCA's disaggregation proposals in the Service Quality Modifications Order, it indicated that the issue might be revisited in this proceeding.<sup>696</sup> That issue is, however, still before the Commission on application for review, and other service quality and infrastructure reporting matters are also pending before us.<sup>697</sup> We will, therefore, adopt ICA's suggestion and defer any changes to the service quality and infrastructure monitoring programs to the separate proceedings that are specially focused on those issues.

366. None of the commenting parties addressed network reliability issues. Since the Notice was issued, the Commission has dealt with those issues in a separate proceeding.<sup>698</sup>

#### G. Other

367. The Common Carrier Bureau recently rescheduled the filing date for the price cap LECs' 1995 annual access filings from March 31, 1995, to 30 days after the release date of this

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<sup>696</sup> Service Quality Modifications Order, 8 FCC Rcd at 7476.

<sup>697</sup> See Policy and Rules Concerning Rates for Dominant Carriers, 6 FCC Rcd 2974 (Com. Car. Bur. 1991) (Service Quality Order), recon., 6 FCC Rcd 7482 (Com. Car. Bur. 1991); Service Quality Modifications Order, 8 FCC Rcd 7474; TCA Application for Review, filed June 17, 1991; International Communications Association ("ICA") and Consumer Federation of America ("CFA") Joint Petition for Rulemaking, filed April 6, 1992; Petitions for Reconsideration of the Common Carrier Bureau's Service Quality Modifications Order filed on November 12, 1993 by the following parties: Ameritech, Bell Atlantic, Pacific Bell and Nevada Bell, Southern New England Telephone Company, Southwestern Bell Telephone Company, United States Telephone Association, and US WEST; US WEST Petition for Limited Waiver of the Commission's ARMIS service quality and infrastructure reporting requirements, filed November 12, 1993.

<sup>698</sup> Amendment of Part 63 of the Commission's Rules to Provide for Notification by Common Carriers of Service Disruptions, CC Docket No. 91-273, Second Report and Order, 9 FCC Rcd 3911 (1994) (Service Disruption Order).

Order. The effective date of the price cap LECs' annual access tariffs was also rescheduled from July 1, 1995, to August 1, 1995.<sup>699</sup> As a result, the 1994-95 tariff period for these carriers will be composed of 13 months, and the 1995-96 tariff period for these carriers will include only 11 months. We hereby direct the price cap LECs to make appropriate adjustments to their indexes, to account for these effects caused by rescheduling their 1995 annual access filings. We delegate authority to the Chief of the Common Carrier Bureau for this purpose. The Bureau's Order also should specify the pleading cycle for the tariff filings and what adjustments, if any, are needed for the tariff filing of the National Exchange Carrier Association (NECA) regarding common line costs.<sup>700</sup>

## VI. TRANSITION ISSUES

### A. Overview

368. This Commission has a long history of fostering the development of competition in telecommunications markets. Partly as a result of the Commission's actions, competition today is a fact in both the customer premises equipment and the long distance market. As we move forward, it is our goal to encourage the development of efficient competition in local telephone markets, as well. While local access competition has begun to develop, the LECs continue to exercise a substantial degree of market power in virtually every part of the country, and continue to control bottleneck facilities.<sup>701</sup> We believe that a competitive local market will produce public interest benefits for consumers in the form of lower prices, better service, and a choice of service providers.

369. In the Notice, we designated several issues as "Transition Issues." We intended the comments submitted in response to these issues to develop data and information relevant to fashioning a workable plan for revising the price cap plan in

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<sup>699</sup> 1995 Annual Access Tariffs, United States Telephone Association, Application for Waiver, DA 95-494 (Com.Car.Bur., released Mar. 16, 1995).

<sup>700</sup> Id. at paras. 6, 11.

<sup>701</sup> See generally Time Comments at 3, 9-11; TCG Comments at 3, 16-19; AT&T Comments at i, 8-9; MFS Comments at 37; API Reply at 5; CCTA Reply at 31-33; ALTS Comments at 2; ALTS Reply at 2; Comptel Comments at i, 4; Ad Hoc Comments at 33; MCI Comments at 65; MFS Comments at 52-53; Hyperion Reply at 1; Wiltel Reply at 8; OCCO Comments at 12.

the future as competition develops.<sup>702</sup> In this section we discuss four categories of transition issues: (1) how to reduce or streamline regulation of price cap LECs as competition develops, and how to determine whether competition has reached a level that might warrant streamlined regulation; (2) whether and how to revise the composition of service baskets; (3) whether and how flexibility within the baskets and bands could be increased; and (4) whether the new services rules should be modified. In the Notice, we sought comment on the new service requirements as a baseline issue.<sup>703</sup> Because some commenters addressed the new services issue in connection with the development of competition, we consider the issue here in this section.

370. One of the transition issues specified in the Notice, how frequently to conduct price cap performance reviews, has been addressed in part by our tentative decision to adopt an X-Factor mechanism based on a moving average. Because a moving average X-Factor would be readjusted automatically to account for future increases in LEC productivity, the need for periodic performance reviews would be greatly reduced. Thus, in our analysis of the X-Factor, we have already begun to explore ways to adapt price cap regulation to competition that is likely to develop in the future. As a result, we will not address this issue further in this section. We will raise the issue of periodic review again in the Further Notice of Proposed Rulemaking, however, particularly for other aspects of the price cap plan. In addition, we solicited comments on whether to revise service quality and infrastructure monitoring as part of a transition price cap plan.<sup>704</sup> We have addressed this issue together with our analysis of existing service quality and infrastructure monitoring in Section V.F.<sup>705</sup> Therefore, we will not address this issue further in this section.

## **B. Background and Comments**

### **1. Reducing or Streamlining Regulation of LEC Services**

371. In the Notice, we stated that, if a LEC no longer controls essential "bottleneck" facilities, then that LEC may no longer possess market power, and it might no longer be necessary

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<sup>702</sup> Notice, 9 FCC Rcd at 1705.

<sup>703</sup> Notice, 9 FCC Rcd at 1701-03.

<sup>704</sup> Notice, 9 FCC Rcd at 1706.

<sup>705</sup> See Section V.F. of this Order, supra; see also Service Quality Modifications Order, 8 FCC Rcd at 7476.

to maintain regulations that protect against abuse by a monopoly.<sup>706</sup> Therefore, we asked for comment on a number of issues in this area, including the current state of competition for local exchange and interstate access, and what criteria should be used for determining whether reduced or streamlined regulation should take effect. We also asked under what circumstances will a LEC no longer have control over "bottleneck" facilities, to what extent CAPs or others have the ability to compete with LECs, and what effect LEC entry into related industries, and BOC entry into interLATA marketplaces, should have on the LEC price cap plan. Finally, we solicited comment on regulatory methods for reducing or streamlining price cap regulation.<sup>707</sup>

372. USTA contends that access competition already exists in many markets and will increase rapidly in the near term.<sup>708</sup> USTA recommends creating a three-tier market structure consisting of Initial Market Areas (IMAs), Transitional Market Areas (TMAs), and Competitive Market Areas (CMAs). Increasing pricing flexibility would be allowed as a market area is reclassified from IMA to TMA, and from TMA to CMA, based on the level of effective competition within the area.<sup>709</sup>

373. Under USTA's proposal, each of a LEC's current study areas or pricing zones would be classified as an IMA.<sup>710</sup> A wire center or group of wire centers within an IMA could be reclassified as a TMA when another entity offers substitutable access services within the area served by the wire center or when an operational expanded interconnection arrangement within the wire center become available.<sup>711</sup> TMAs, or parts thereof, could be reclassified as CMAs as each wire center satisfies additional criteria demonstrating increased competition. A TMA could be reclassified as a CMA if, e.g., customers within the serving area of the wire center representing at least 25 percent of the demand for the LEC's interstate access services (1) have available to them an alternative source of supply; and (2) solicit bids to reduce the cost of their access services.<sup>712</sup> Services in a CMA

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<sup>706</sup> Notice, 9 FCC Rcd at 1705.

<sup>707</sup> Id.

<sup>708</sup> USTA Comments at 24, 39.

<sup>709</sup> USTA Comments at 58.

<sup>710</sup> USTA Comments at 59.

<sup>711</sup> USTA Comments at 64-65.

<sup>712</sup> USTA Comments at 33-39, 62-65.

would be removed from price cap regulation.<sup>713</sup>

374. MCI avers that the Commission recently rejected a USTA plan similar to USTA's three-tiered market structure proposal in this proceeding and that nothing has changed since that decision that would support a change of course now.<sup>714</sup>

375. In response to USTA's January 18 proposal, NYNEX recommends that the Commission establish a series of sharing bands that would link the elimination of sharing requirements with local exchange competition.<sup>715</sup> In a subsequent ex parte filing, NYNEX proposes a three-stage plan that would relax sharing requirements for LECs that have implemented measures to promote local exchange competition (e.g., unbundled local loop offerings).<sup>716</sup>

376. Bell Atlantic and Ameritech state that their interstate intraLATA toll and corridor interexchange services face intense competition and should be removed from price cap regulation.<sup>717</sup> Bell Atlantic and SNET state that their high capacity (DS1 and DS3) access services and video dialtone services face intense competition and should be removed from price caps.<sup>718</sup>

377. MFS recommends that, once the bottlenecks are opened on a nondiscriminatory basis to competitors, greater pricing flexibility be allowed based on a showing by the LEC that

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<sup>713</sup> USTA Comments at 69-70; see also GTE Comments at 47-58 (supporting USTA's three-tier market proposal); id. at 47 (stating that "the main focus of the Commission's access market definition should be geographic in nature, and that the unit of observation chosen should be the smallest practical geographic area").

<sup>714</sup> MCI Reply at 22, citing Expanded Interconnection with Local Telephone Company Facilities, 7 FCC Rcd 7369 (1992), 7 FCC Rcd 7374, 7426-28 (1993); id. (stating that as recently as May 27, 1994, the Commission stated that there is no present need to expand the scope of LEC pricing flexibility, because to do so would threaten emerging competition) (citing Expanded Interconnection with Local Telephone Company Facilities, 8 FCC Rcd 2718 (1994)).

<sup>715</sup> NYNEX January 18 Comments at 5.

<sup>716</sup> NYNEX March 3 Proposal at 4.

<sup>717</sup> Bell Atlantic Comments at 19-20; Ameritech Comments at 29-30.

<sup>718</sup> Bell Atlantic Comments at 1-3, Affidavit of Richard E. Beville at 15; SNET Comments at 13.

competitive services are actually available on a widespread basis throughout the geographic area.<sup>719</sup> TCG maintains that the Commission should consider additional flexible regulation of LECs when competition reaches the levels that AT&T experienced when the Commission deregulated AT&T's services.<sup>720</sup>

378. Sprint proposes that the Commission adopt a 3.3, a 3.9, and a 4.5 percent X-Factor.<sup>721</sup> LECs choosing the 4.5 percent X-Factor would qualify for more streamlined regulation and greater pricing flexibility, including immediate implementation of zone density pricing.<sup>722</sup>

## **2. Revising Baskets**

379. When we created the price cap baskets for LECs, each with separate price cap indexes and bands, we balanced two competing concerns. First, we limited the number of baskets to ensure that the company-wide productivity offset would be appropriate for each basket. Second, because we wanted to preclude LECs from disadvantaging customers for one service with higher prices so that it could lower prices charged to another service class, we based the baskets on existing access categories.<sup>723</sup> In addition, we grouped similar services into service categories within some baskets, to limit the LECs' ability to shift costs between services in a potentially anticompetitive manner.<sup>724</sup> We have made some revisions to the

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<sup>719</sup> Specifically, MFS would require the price cap LEC to show that 50 percent of customers have competitive services available and that 15 percent actually use those services. MFS Comments at 44. MFS's suggested standard is similar to the definition of "effective competition" incorporated in the Cable Act of 1992. Section 623(1)(1) of the Communications Act, 47 U.S.C. § 623(1)(1).

<sup>720</sup> TCG Comments at 11.

<sup>721</sup> Sprint Dec. 29, 1994 Ex Parte Proposal; Sprint Feb. 2, 1995 Ex Parte Proposal.

<sup>722</sup> Sprint Dec. 29, 1994 Ex Parte Proposal; see also id. (for LECs electing the 4.5 percent X-Factor, 1.7 percent would be "targeted to transport RIC phasedown, .8 percent effected through adoption of the per line cap for the [carrier common line charge], and a 2 percent productivity offset applicable to all baskets").

<sup>723</sup> LEC Price Cap Order, 5 FCC Rcd at 6812.

<sup>724</sup> LEC Price Cap Order, 5 FCC Rcd at 6811.



price cap baskets during the first four years of the plan.<sup>725</sup> Currently, the common line and interexchange baskets have no service categories.<sup>726</sup> The traffic sensitive switched basket contains separate service categories for local switching, information, database access, and billing name and address (BNA).<sup>727</sup> The trunking basket currently contains separate service categories for (i) voice grade entrance facilities; (ii) audio and video services; (iii) high capacity special access services, with subcategories for DS1 and DS3 services; (iv) wideband data and wideband analog services; (v) tandem-switched transport; (vi) interconnection charges; and (vii) signalling for tandem switching.<sup>728</sup> In the Notice, we stated that it might be necessary to revise the price cap baskets to group services with similar levels of competition together. We solicited comment on whether and how the Commission should schedule revisions to baskets as competition develops.<sup>729</sup>

380. USTA proposes that four baskets be established within the price cap plan: transport,<sup>730</sup> switching,<sup>731</sup> "Public

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<sup>725</sup> See Transport Rate Structure and Pricing, CC Docket No. 91-213, Second Report and Order, 9 FCC Rcd 615 (1994) (Second Transport Order); see also Transport Rate Structure and Pricing, CC Docket No. 91-213, Report and Order and Further Notice of Proposed Rulemaking, 7 FCC Rcd 7006 (1992) (Transport Order); 8 FCC Rcd 5370 (1993) (First Transport Reconsideration Order); 8 FCC Rcd 6233 (1993) (Second Transport Reconsideration Order); Provision of Access for 800 Service, CC Docket No. 86-10, 8 FCC Rcd 907 (1993); Policies and Rules Concerning Local Exchange Carrier Validation and Billing Information for Joint Use Calling Cards, CC Docket No. 91-115, Second Report and Order, 8 FCC Rcd 4478 (1993) (BNA Order), recon. 8 FCC Rcd 6393 (1993); further recon. 8 FCC Rcd 8978 (1993), recon. pending.

<sup>726</sup> Section 61.42(d) of the Commission's Rules, 47 C.F.R. § 61.42(d).

<sup>727</sup> Section 61.42(e)(1) of the Commission's Rules, 47 C.F.R. § 61.42(e)(1).

<sup>728</sup> Section 61.42(e)(2) of the Commission's Rules, 47 C.F.R. § 61.42(e)(2).

<sup>729</sup> Notice, 9 FCC Rcd at 1705-06.

<sup>730</sup> The Transport basket would include all interoffice transport, all facilities provided under interstate access tariffs between the local serving office and a customer's premises, any features associated with transport, and the interconnection charge. USTA Comments at 67.

Policy,"<sup>732</sup> and "Other," to include any rate elements that did not fit into the other baskets.<sup>733</sup> Within a basket, USTA would establish separate market area categories corresponding to the maximum number of IMAs established in any study area or zone. One TMA market area category would be established for all TMA elements within the Transport, Switching and Other baskets. IMA and TMA category designations would not apply to the Public Policy basket.<sup>734</sup>

381. Although many of the LECs support USTA's proposal for restructuring the current price cap basket structure,<sup>735</sup> some of the LECs make their own recommendations for revising the basket and band structure to increase pricing flexibility.<sup>736</sup> For

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<sup>731</sup> The switching basket would include all current and new switching functions, as well as features associated with switching. USTA Comments at 68.

<sup>732</sup> The Public Policy basket would include Lifeline Assistance, Universal Service Fund, End-User Common Line Charge, Carrier Common Line Charge (or a substitute recovery mechanism), Long-Term Support, Interconnection Charge, Telecommunications Relay Service, Special Access Surcharge, and any other elements established by the Commission for explicit interstate public policy purposes. USTA Comments at 68.

<sup>733</sup> USTA Comments at 68; see also January 18 Letter, Attachment 2 at 3.

<sup>734</sup> USTA Comments at 68.

<sup>735</sup> USTA Comments at 66-72; SWB Comments at 86; Lincoln Comments at 13; RTC Comments at 13-14; NYNEX Comments at 25; see generally SNET Comments at 11.

<sup>736</sup> See US West Comments at 30, 88-89; id. at 31 n.66 (US West supports USTA's proposal, but believes it is overly conservative in restricting the downward pricing flexibility in IMA and TMA sub-indexes); see generally Pac Bell Comments at 102 (although Pac Bell supports USTA's proposal, Pac Bell believes that ultimately there should be only two baskets: one basket for services subject to explicit and implicit subsidies, and another for services that are subject to high elasticities of supply and demand, but are not fully competitive); NYNEX Comments at 26-27 (as an alternative to USTA's proposal, recommends reducing the categories in the Trunking basket to two: one for analog and another for digital). NYNEX also asserts that Billing Name and Address (BNA) is a billing and collection service, and that it should be removed from price cap regulation. NYNEX Comments at 26-27. We have determined previously that BNA is not a billing and collection service, and we will not revisit that issue at this time. See BNA Order, 8 FCC Rcd

example, BellSouth recommends renaming the interexchange basket "Other," and expanding it to include all new services that "cannot be appropriately assigned to the [other three baskets.]"<sup>737</sup> BellSouth also proposes reducing the service categories in the Trunking basket to three: Tandem-switched Transport and Interconnection, which would be subdivided into two subcategories: High Capacity services (including DDS) and "Other."<sup>738</sup> BellSouth recommends similar streamlining of the service categories in the Traffic Sensitive basket.<sup>739</sup>

382. MCI, Ad Hoc, ICA, and TCG contend that the basket and band rules should not be revised at this time and assert that the current composition of baskets gives the LECs adequate pricing flexibility to respond to any emerging competition.<sup>740</sup> MCI asserts that USTA's proposal to reduce the number of service categories would provide the LECs with unwarranted pricing flexibility.<sup>741</sup> MCI also notes that the Commission recently declined to move transport switching into the switching basket because would allow LECs to mix non-competitive local switching with potentially competitive tandem switching.<sup>742</sup>

### **3. Service Category Band Flexibility**

383. Each price cap basket is subject to an aggregate price cap or ceiling. A presumption of lawfulness and relatively short tariff filing notice periods apply to rate changes that do not result in the aggregate rates for each basket exceeding the price cap. Within two of the baskets (traffic sensitive and trunking), specific LEC services are grouped into narrower service categories and subcategories, each of which is subject to upper and lower pricing bands (i.e., aggregate price ceilings and

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at 4480-82.

<sup>737</sup> BellSouth Comments at 25.

<sup>738</sup> Id.

<sup>739</sup> Id.

<sup>740</sup> Ad Hoc Comments at 18; TCG Comments at 11; MCI Comments at 16; ICA Reply at 11.

<sup>741</sup> MCI Reply at 22.

<sup>742</sup> MCI Reply at 23, citing Second Transport Order, 9 FCC Rcd 615. MCI also contends that there are a number of petitions pending before the Commission to revise the access charge rate structure, and asserts that it would be premature for the Commission to modify the price cap structure prior to a resolution of the LEC access service structure. MCI Comments at 18 n.22.

floors). The upper and lower bands for most of the service categories and subcategories are +/- 5 percent relative to the price cap index for the basket.<sup>743</sup> As with the baskets, the presumption of lawfulness and relatively short tariff filing notice periods apply to rate changes as long as the aggregate rates for each service category and subcategory remain between the upper and lower pricing bands. Substantial cost justification and longer tariff filing notice periods are required if rates exceed the price cap for a basket or fall above or below the applicable pricing bands for a service category or subcategory.

384. We adopted the service category lower bands as a check against predatory pricing. LECs filing tariffs with rates below the applicable lower bands for a service category must demonstrate that their revised rates are above average variable costs. We also intended to limit the LECs' ability to offset rate reductions in some categories with rate increases in other categories. In the Notice, we invited interested parties to discuss whether and how we should adopt changes in these rules and policies as part of a LEC price cap transition plan.<sup>744</sup>

385. Under USTA's proposal, individual IMA and TMA categories would be subject to an upper pricing band of 5 percent per year, and lower pricing bands of 10 percent and 15 percent, respectively.<sup>745</sup> Also, USTA recommends shorter notice periods and streamlined cost support requirements based on the level of effective competition within the area.<sup>746</sup>

386. In its January 18 ex parte statement, USTA advocates eliminating the DS1 and DS3 subindexes, expanding the lower banding limits to minus 15 percent, and extending zone pricing to the local switching category as well as to all elements in the

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<sup>743</sup> Certain service categories have narrower upper bands and/or broader lower bands. Specifically, the tandem switched transport service category has a +2 percent upper band and a -5 percent lower band; the transport interconnection charge service category has a +0 percent upper band and no lower band; and the signalling for tandem switching service category has a +2 percent upper band and no lower band.

<sup>744</sup> Notice, 9 FCC Rcd at 1706.

<sup>745</sup> USTA Comments at 69.

<sup>746</sup> USTA Comments at 77-78; see also NYNEX Comments at 19 and 20 n.50 (although NYNEX supports USTA's proposal, it recommends significantly greater flexibility for many services offered in TMAs and IMAs).

trunking category except the interconnection charge.<sup>747</sup>

387. NYNEX and Ameritech suggest that, if banding is retained for all Trunking services, each service category and zone should be subject to an upper pricing band of 5 percent and a lower pricing band of at least 15 percent to allow downward flexibility in competitive zones and for digital services.<sup>748</sup> In addition, NYNEX recommends that the banding limits on local switching, directory and database should be modified to permit rate decreases of up to 10 percent without cost support.<sup>749</sup> Ameritech recommends that the Commission establish zone density pricing for local switching with an upper pricing band of 5 percent and a lower pricing band of 15 percent.<sup>750</sup>

388. BellSouth recommends increasing the downward pricing flexibility based on its proposed basket restructure, discussed above. BellSouth would place an upper and lower banding limit of 5 percent on the Dedicated Service Transport category; a 15 percent lower pricing limit for the High Capacity and "Other" subcategories of the Transport services category and for the Information and Database categories; and a 10 percent lower pricing limit for zone pricing in the trunking basket. In addition, BellSouth proposes extending zone pricing to the switched service category, with upper and lower pricing limits identical to those in the trunking basket.<sup>751</sup> MCI replies that there have been no changes in the marketplace since the adoption of zone pricing and the recent restructure of the bands and baskets to warrant adoption of BellSouth's proposal for modifying the LEC price cap basket and band structure.<sup>752</sup>

389. WilTel and MFS assert that the current price cap baskets and bands do not constrain the LECs' ability to offset price decreases for more competitive services with price increases for less competitive services, thus allowing LECs to implement unreasonably discriminatory rate relationships. WilTel recommends that the Commission "address discrimination in rate

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<sup>747</sup> January 18 Letter, Attachment 2 at 2.

<sup>748</sup> NYNEX Comments at 26-27; Ameritech Reply at 10-11.

<sup>749</sup> NYNEX Comments at 26-27.

<sup>750</sup> Ameritech Reply at 10-11.

<sup>751</sup> BellSouth Comments at 25-31.

<sup>752</sup> MCI Reply at 23-24.

relationships by adopting cost-based pricing principles . . .  
..<sup>753</sup> MFS recommends that the Commission require rates in the trunking basket to be set equal to incremental costs, plus an allocation of overhead costs that would be based on the same loading factor for all rate elements in the trunking basket.<sup>754</sup>

390. The LECs make several arguments to rebut WilTel's and MFS's claims: 1) there is no discrimination because different prices are not being charged to similarly situated customers for like services; 2) a fully allocated cost approach to rate setting is inconsistent with price cap regulation;<sup>755</sup> and 3) MFS's cost consistency proposal would constitute a reversion to rate-of-return regulation, ignores market demand information, and would be an enormous administrative burden.<sup>756</sup>

391. Comptel claims that tandem-switched transport service should be in the switching basket, because tandem and local switching functions generally are performed by the same switch, and that tandem-switched rates should be based on DS1 and DS3 rates.<sup>757</sup> Comptel maintains that, because tandem switching is now in the trunking basket, the LECs are able to allocate excessive overhead amounts to tandem switching. Comptel maintains that this distorts interexchange competition, because tandem switching is used predominantly by smaller IXC's.<sup>758</sup>

392. In response to Comptel's arguments and proposal, Pac Bell says that tandem switching rates do not subsidize local

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<sup>753</sup> WilTel Comments at 18-23; see also id. at 22 (WilTel suggests that the Commission "could conduct cost studies in an effort to reset the starting point for rates for all price cap services"); Comptel Comments at 9-14 (claiming that an excessive proportion of overhead costs are recovered through DS1 rates relative to DS3 rates).

<sup>754</sup> MFS Comments at 15-21. Alternatively, MFS recommends adoption of rate-element banding in the trunking basket under which no individual rate element could be increased or decreased by more than 5 percent annually relative to the PCI, except for those elements with special pricing rules such as the interconnections charge. Id. at 20 n.17.

<sup>755</sup> BellSouth Reply at 11-14; Pac Bell Reply at 41 (asserting that the Commission is not required to mandate the allocations that WilTel proposes).

<sup>756</sup> NYNEX Reply at 16; Pac Bell Reply at 53; SWB Reply at 73.

<sup>757</sup> Comptel Comments at 11.

<sup>758</sup> Comptel Comments at 11-15.

switching rates but, rather, as a result of the Commission's decision in CC Docket No. 91-213, usage-based transport rates subsidize tandem switching rates.<sup>759</sup> Pac Bell notes that the Commission observed that "a ban on discounts would disadvantage the LECs without providing small IXCs the benefits they seek to achieve."<sup>760</sup> Pac Bell asserts that the Commission has already decided against requiring rate relationships between DS1 and DS3.<sup>761</sup>

#### 4. New Services

393. The LEC Price Cap Order defines new services as services that add to the range of options already available to customers. A new service may, but need not, include a new technology or functional capability.<sup>762</sup> New services are not included under the price cap indexes until the first annual price cap tariff filing after the completion of the base year in which the new service becomes effective.<sup>763</sup>

394. Under our current rules, tariff filings proposing new services that will be subject to LEC price caps must be made on at least 45 days' notice<sup>764</sup> and be accompanied by "detailed cost support[.]"<sup>765</sup> Specifically, a LEC introducing a new service is required to show that it has used a consistent costing methodology for direct costs "for all related services."<sup>766</sup> Cost support accompanying a LEC new service tariff filing must include, in part, a study containing a projection of costs for a representative 12-month period and estimates of the effect of the new service on traffic and revenues, including the traffic and revenues of other services.<sup>767</sup> As part of the justification for

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<sup>759</sup> Pac Bell Reply at 33-34.

<sup>760</sup> Pac Bell Reply at 35, quoting Expanded Interconnection with Local Telephone Company Facilities, CC Docket No. 91-141, 8 FCC Rcd 7374, 7434 (1993).

<sup>761</sup> Pac Bell Reply at 37, citing Second Transport Order, 9 FCC Rcd at 623.

<sup>762</sup> LEC Price Cap Order, 5 FCC Rcd at 6824.

<sup>763</sup> LEC Price Cap Order, 5 FCC Rcd at 6824.

<sup>764</sup> Id. at 6825.

<sup>765</sup> Part 69 ONA Order, 6 FCC Rcd at 4524.

<sup>766</sup> Part 69 ONA Order, 6 FCC Rcd at 4531.

<sup>767</sup> Part 69 ONA Order, 6 FCC Rcd at 4531.

the price selected for the new service, LECs may include "risk premium" on investments in unusually risky new services.<sup>768</sup>

395. To derive the overall price of the new service, LECs add a "reasonable" level of overhead costs.<sup>769</sup> LECs may load overhead on new services in a non-uniform manner, provided that LECs justify the deviations from uniform loadings.<sup>770</sup> Where a LEC develops a lower cost version of an existing service, pricing the service so that the LEC breaks even would be an acceptable justification for non-uniform loadings.<sup>771</sup> Further, non-uniform overhead loadings are presumptively reasonable whenever a LEC uses them to justify the introduction of a new service at a level below the imputed "old" price of a substitutable service.<sup>772</sup>

396. In light of our concern that the LECs may understate the direct costs of video dialtone service in order to set unreasonably low prices and engage in cross-subsidization, we provided in the Video Dialtone Order more specific guidance regarding the identification of direct costs in video dialtone new service tariff filings than we have given for other new services filings.<sup>773</sup> In particular, LECs are required to include in direct costs a reasonable allocation of common costs associated with shared plant used to provide video dialtone and other services. LECs allocating an extremely low percentage of common costs of shared plant to video dialtone must provide a strong justification for doing so. In addition, LECs are required to provide a strong justification for allocation of extremely low overheads to video dialtone service.<sup>774</sup>

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<sup>768</sup> Part 69 ONA Order, 6 FCC Rcd at 4531; see also Second Further Reconsideration, 7 FCC Rcd at 5237 (a risk premium is "defined as the additional rate of return a LEC needs to justify the development of a particularly risky new service").

<sup>769</sup> Part 69 ONA Order, 6 FCC Rcd at 4531.

<sup>770</sup> Part 69 ONA Order, 6 FCC Rcd at 4531.

<sup>771</sup> Second Further Reconsideration, 7 FCC Rcd at 5236; Third Further Reconsideration at para. 5.

<sup>772</sup> Second Further Reconsideration, 7 FCC Rcd at 5237; Third Further Reconsideration at para. 5.

<sup>773</sup> Telephone Company-Cable Television Cross Ownership Rules, Section 63.54-63.58, CC Docket No. 87-266, and Amendments of Parts 32, 36, 61, 64, and 69 of the Commission's Rules to Establish and Implement Regulatory Procedures for Video Dialtone Service, RM-8221, 10 FCC Rcd 244, 344-46 (1994) (Video Dialtone Order).

<sup>774</sup> Id. at 345-46.



397. In our Notice, we asked whether the LEC price cap new services requirements impose unnecessary regulatory impediments to the development and introduction of new services and, if so, how we should modify the LEC price cap new services procedures and cost support rules to ensure that these rules advance our goals of encouraging innovation and setting reasonable rates. We also asked whether new services are available on an equal basis to all LEC customers and whether we should revise the LEC price cap plan to ensure the universal availability of new services.

398. USTA and the LECs contend that the LEC price cap new services rules, the Part 69 rate structure requirements, and the constraints on pricing flexibility impede the development and introduction of new services.<sup>775</sup> Some of these commenters claim that the new services rules require an unnecessarily long notice period, as well as complex and detailed cost support.<sup>776</sup> They maintain that many new services do not readily fit the Part 69 rate structure requirements and that the process for obtaining a waiver or changing the rules for new switched access services is costly, time-consuming, and highly uncertain.<sup>777</sup>

399. USTA and some of the LECs propose that the Commission revise the Part 69 rules to codify only those elements that are necessary to implement a specific public policy program established by the Commission.<sup>778</sup> Moreover, USTA's three-tier market structure proposal, discussed above, would require the Commission to revise the new services rules by adopting a regulatory mechanism which allows for streamlined cost support requirements and shorter notice periods based on the degree of

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<sup>775</sup> USTA Comments at 52; Ameritech Comments at 8; GTE Comments at 10, 18; SWB Comments at 78-80; US West Comments at 52; SNET Comments at 3; Lincoln Comments at 13; Ameritech Comments at 21-22; BellSouth Comments at 60-61; NYNEX Comments at 41; Pac Bell Comments at 64; Bell Atlantic Comments at 28; see also ICA Comments at 19-20; US West at 54 (stating that the Part 61 prohibition on references to technical publications in tariffs impedes the introduction of new services; Section 61.74 of the Commission's Rules should be modified to permit LECs to reference technical publications in their interstate tariffs).

<sup>776</sup> US West Comments at 52, 57; USTA Comments at 23; GTE Comments at 10; SWB Comments at 80; NYNEX Comments at 42; SNET Comments at 3; Ameritech Comments at 23.

<sup>777</sup> USTA Comments at 52-53; US West Comments at 52; SWB Comments at 73; Pac Bell Comments at 64; SNET Comments at 3; GTE Comments at 10-12.

<sup>778</sup> USTA Comments at 18, 72-77; SWB Comments at 79-81; RTC Comments at 15; Pac Bell Comments at 64; GTE Reply at 62-68.